

Changes in Ownership Structure and Real Investors¹

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Introduction

Higher equity holding by investors causes their right of vote to have more weightage in shareholder meetings. In other words, those who hold many shares have a significant impact on the company. When studying management of incorporated companies, one needs to consider the big picture of ownership structure. Today, foreign institutional investors hold majority of Japan's publicly listed stocks; Japanese institutional investors hold a significant percentage as well. And many Japanese institutional investors have signed Japan's Stewardship Code. However, securities filings identify Japan Trustee Services Bank and The Master Trust Bank of Japan as major shareholders because institutional investors often assign their shares to trustees who provide services to their institutional clients.

The present study examines the following: How do these investors exercise voting, and how do they have a dialogue with investee companies in order to fulfill their stewardship responsibility? Who drafts the voting policy, votes on shareholder measures, and has a dialogue when institutional investors entrust their custody?

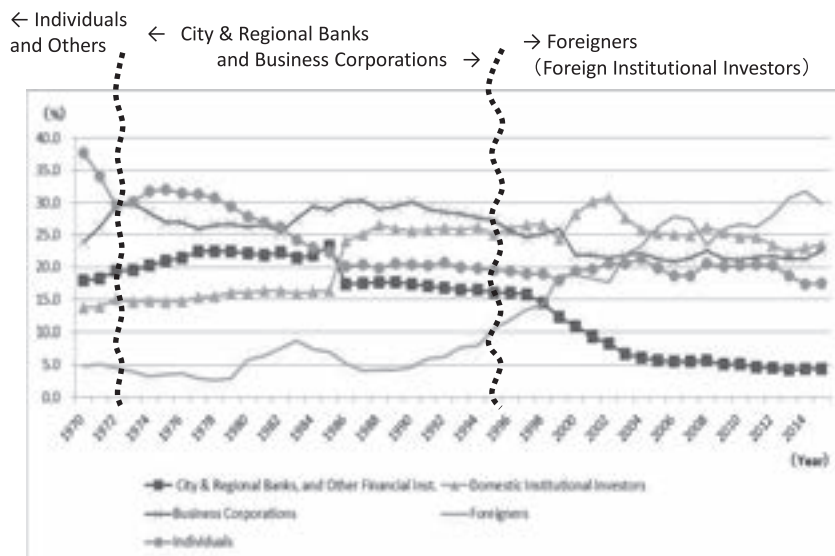
¹ This paper is based on articles originally published as Yosuke Torii, "Stewardship Responsibilities of Real Investors and Voting Activities: Surveying Institutions That Signed Up for Japan's Stewardship Code", *Journal of Business Management*, No. 39 (2017a), pp. 61–72; "Trustees as Major Shareholders and their Voting Activities in Japan", In Tsuneo Sakamoto and Shigeru Shoda (Eds.), *Global, Innovative and Environmental Management*, Maruzen Planet (2017b), pp. 98–112; and "Structure and Position of Trust Accounts as Major Shareholders in Japan", *Annals of Society for the Economic Studies of Securities*, No. 51 (2016), pp. 49–59.

1. History of Ownership Structure in Japan

Figure 1 shows the history of ownership structure in Japan. In pre-World War II Japan, family-run conglomerates called *zaibatsu* capitalized on and controlled wholly owned business subsidiaries. After the war, Japan's governing military headquarters dissolved all *zaibatsu*. When threatened by hostile takeovers or capital liberalization, *zaibatsu* formed cross-shareholdings with affiliated companies in their groups. During this period, banks were the major shareholders and companies were affiliated with the same group; therefore, companies were managed for the benefit of their groups and to gain market share.

The bursting of Japan's economy bubble led to the plummeting of stock prices and the dissolving of cross-shareholdings following the introduction of market-value accounting. Foreign institutional investors bought large numbers of equities sold by banks and corporations. They have made a request shareholder return to companies and have evaluated companies using an index such as return on equity (ROE).

Figure 1 Shareholding at Market Value in Japan



(Notes) 1. Foreigners: Non-Japanese corporations and individuals (including foreign trust banks)

2. The number of domestic institutional investors rose dramatically from 1985 to 1986 because of changes in the method of totalization.

(Source) Japan Stock Exchange "2015 Shareownership Survey"

Institutional investors presently own the highest percentage of Japan's publicly listed stocks. However, securities filings identify Japan Trustee Services Bank, The Master Trust Bank of Japan, and Trust & Custody Services Bank as the major shareholders (see Figure 2). This is because institutional investors often assign their shares to trustees that manage several tasks for their institutional clients. These institutions are called specialized asset administration banks (SAABs).

Who are the real investors? Real investors include investment trusts, pension funds, and public institutions. How do these real investors (institutional investors) affect investee companies?

Sakamoto (1998) regard Japanese institutional investors of the late 1990s as instruments of commercial banks.

Basically, major commercial banks determine the fund management activities of Japanese institutional investors. This is because they played a leading role in regrouping business groups dissolved by GHQ after World War II. And in insurance companies, for example, their clients are related business group companies controlled by major commercial banks. Therefore, insurance companies have to obey major commercial banks when they invest capital raised as insurance.

During the later 1990s, Japanese institutional investors differed from foreign institutional investors, who strove to out-perform each other.

Many studies suggest poor Japanese corporate governance. Many Japanese shareholders are regarded as stable shareholders because they do not exercise voting rights. The doubt arises whether institutions that entrust their custody exercise their voting rights well.

Figure 2 Ten Largest Shareholders of Toyota Motor Corporation

Names	Number of shares held (thousands of shares)	Percentage of total (%)
Japan Trustee Services Bank, Ltd.	358, 791	10. 60
Toyota Industries Corporation	224, 515	6. 63
The Master Trust Bank of Japan, Ltd.	149, 005	4. 40
Nippon Life Insurance Company	120, 390	3. 56
State Street Bank and Trust Company (standing proxy: Settlement & Clearing Services Division, Mizuho Bank, Ltd.)	115, 230	3. 40
DENSO CORPORATION	86, 513	2. 56
JP Morgan Chase & Company (standing proxy: Settlement & Clearing Services Division, Mizuho Bank, Ltd.)	73, 483	2. 17
The Bank of New York Mellon as Depositary Bank for Depositary Receipt Holders	66, 933	1. 98
Trust & Custody Services Bank, Ltd.	64, 005	1. 89
Mitsui Sumitomo Insurance Company, Limited.	62, 063	1. 83

(Note) As of March 31, 2016.

(Source) Toyota Motor Corporation Homepage,

http://www.toyota-global.com/investors/stock_information_ratings/outline.html.

2. Formulation of Japan's Stewardship Code and "Stewardship Responsibility"

In February 2014, Japan enacted a Stewardship Code that prescribed a set of principles governing the actions of institutional investors. They include constructive engagement with companies and voting. This code "defines principles considered to be helpful for institutional investors who behave as responsible institutional investors in fulfilling their stewardship responsibilities with due regard both to their clients and beneficiaries and to investee companies."²

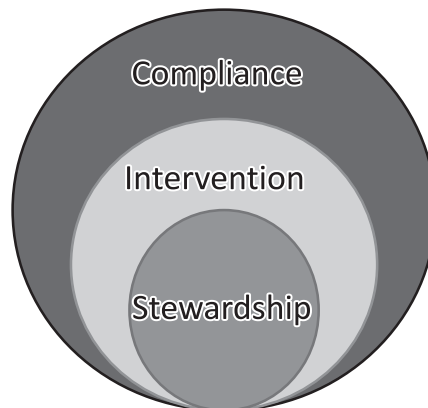
What are "stewardship responsibilities" ? They "refer to the responsibilities of in-

² The Council of Experts Concerning the Japanese Version of the Stewardship Code (2014), P1.

stitutional investors to enhance the medium- to long-term investment return for their clients and beneficiaries (including ultimate beneficiaries; the same shall apply hereafter) by improving and fostering the investee companies' corporate value and sustainable growth through constructive engagement, or purposeful dialogue, based on in-depth knowledge of the companies and their business environment.”³

Winter (2011) states that “the stewardship variant of engagement goes yet further. In that variant the engagement is structural, not limited in time or to a certain problem. The structural engagement is in fact there to add value to the investment in the long term; it is the crux of a different way of investing. Shares are held for longer periods and success is determined on a long-term basis. Not continuously using the exit option that the market offers requires greater involvement of the investor in the company, more understanding, more information, and exercising more influence to protect and increase the value of the investment.”⁴

Figure 3 Levels of Engagement by Institutional Investors



(Source) Winter (2011), P12.

The reason why Japan's Stewardship Code requests “stewardship responsibility” is because institutional investors have a significant impact on the investee companies. In the current Japanese stock market, foreign institutional investors account for more than 30%. However, the number of Japanese institutional investors is also growing.

Using financial data, Iwatsubo and Sotoki (2007) and Miyajima and Hoda (2015)

³ Id.

⁴ Winter (2011), P12.

clarified that both foreign and Japanese investors affect corporate value and performance. However, it is unknown if this influence results from engagement, voting activities, or other reasons.

The present study reveals institutional investors' activities through published voting data and the results of questionnaires from institutional investors who accepted Japan's Stewardship Code and suggests that these investors foster the investee companies' corporate value and sustainable growth through constructive engagement, voting, or purposeful dialogue.

3. Flow of Voting Activities and Voting Records of Real Investors

Voting activity is one method by which institutional investors affect investee companies. They need to vote properly to fulfill their stewardship responsibility. It is imperative that we know who sets the voting policy and votes on shareholder measures because securities filings identify Japan Trustee Services Bank and The Master Trust Bank of Japan as the major shareholders. The study investigated the voting method and the dialogue process when institutional investors entrust administration by submitting a questionnaire to institutional investors who had accepted Japan's Stewardship Code.

This questionnaire surveyed 194 institutional investors who had accepted Japan's Stewardship Code. A total of 162 candidates were surveyed in Japan; 32 candidates, whose headquarters were overseas, were not subjected to the survey. Of the 162 candidates surveyed in Japan, 30 institutional investors responded.

Figure 4 Comparison between Universe and Sample

Classification		Relative Frequency			
		Universe		Sample	
Asset Manager	Investment managers	141	72.7%	22	73.3%
	Trust banks	7	3.6%	2	6.7%
Asset Owner	Pension funds	24	12.4%	5	16.7%
	Insurance companies	22	11.3%	1	3.3%
Total		194	100%	30	100%

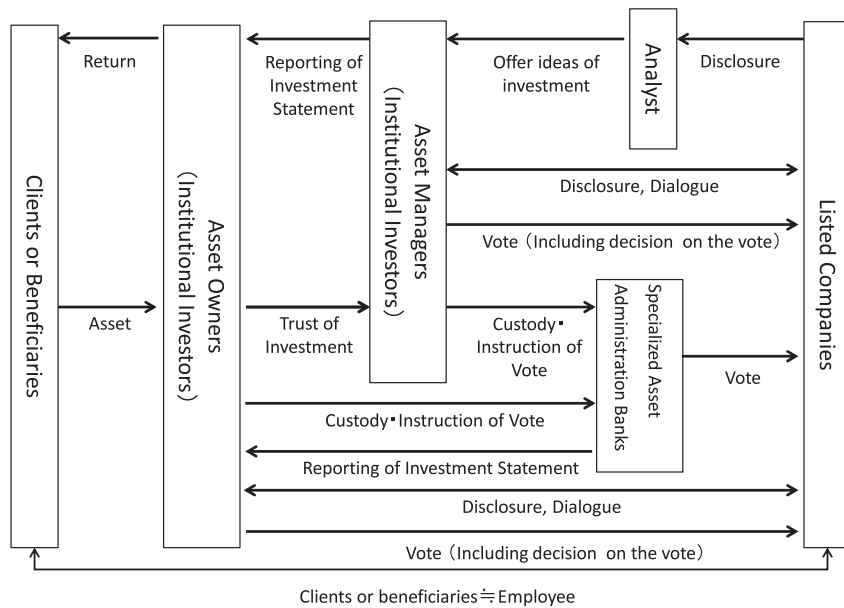
(Note) Investigation period: January 2016-March 2016

Collection rate: 18.5%

First, the questionnaire investigated how institutional investors manage and administer stocks and exercise their voting. Many asset owners (e.g., pension funds) entrust their asset management and votes. Asset managers judge bills based on the voting policy that the asset owners have. Sometimes asset managers refer to the opinions of service providers.

Many asset managers deliver yeas and nays to SAABs, and they complete the voting forms and votes. Although many asset owners entrust their voting activities to asset managers, they check if the trustees judge each bill properly.

Figure 5 Flow of Voting Activities and the Investment Chain



(Source) Kitagawa (2015), P1; Oguchi (2016).

Figure 6 displays the voting records of institutional investors who adopted Japan's Stewardship Code in 2014 and 2015. On average, 11.91% and 10.36%, respectively, of the votes cast dissented to the approval of a proposed measure.

Many institutional investors cast dissenting votes in 2014 and 2015. One way to assess whether this percentage is high is to compare it with the dissenting votes during the era when silent partners with extensive cross-shareholdings were the largest group of Japanese shareholders. Unfortunately, there is lack of data on past voting records. However, almost all shareholder meetings during that era were concluded within 30 minutes, so we can infer that few dissenting votes were cast. Compared with that era, 11.91% and 10.36% dis-

senting votes appear quite substantial.

These figures indicate that the higher percentage of dissenting votes was a result of takeover defenses, payment of retirement benefits, and other measures. The category “other measures” includes acquiring treasury stock, reducing legal reserves, allocating new shares to third parties, reducing capital, and approving reverse stock splits. Institutional investors apparently followed guidelines to vote against measures that might impair shareholder returns. Both foreign investors and Japanese institutional investors exercise voting rights.

Figure 6 Voting Records of Institutional Investors who Adopted Japan’s Stewardship Code

Bills	Fiscal year 2014			Fiscal year 2015		
	Affirmative Vote	Dissenting Vote	Abstention	Affirmative Vote	Dissenting Vote	Abstention
Appropriation of retained earnings	96.29%	3.64%	0.07%	95.94%	4.03%	0.02%
Appointment of board members	90.13%	9.80%	0.07%	90.15%	9.81%	0.04%
Appointment of auditors	77.58%	22.35%	0.07%	84.46%	15.52%	0.02%
Alteration of memorandum	96.24%	3.67%	0.09%	95.09%	4.88%	0.03%
Payment of retirement benefits	57.65%	42.02%	0.33%	55.10%	44.83%	0.07%
Revision of board members’ compensation	93.53%	6.04%	0.43%	92.30%	7.67%	0.03%
Issuance of stock acquisition rights	81.32%	18.22%	0.46%	82.52%	17.24%	0.24%
Appointment of accountant auditors	97.21%	2.79%	0.00%	98.67%	0.83%	0.50%
Category of restructuring	91.23%	8.77%	0.00%	97.41%	2.59%	0.00%
Takeover defense	50.85%	49.15%	0.00%	50.39%	49.61%	0.00%
The others	59.49%	40.42%	0.09%	77.94%	22.05%	0.01%
Total	88.05%	11.91%	0.05%	89.56%	10.36%	0.07%

(Notes) 1. Aggregate votes at shareholder meetings in May or June 2014 and 2015.

2. “Category of restructuring” includes mergers, transfers, or acquisitions of businesses, stock swaps, equity transfers, and corporate divestitures.

3. “Other measures” include acquiring treasury stock, reducing legal reserves, allocating new shares to a third party, reducing capital, and approving reverse stock splits.

(Source) Voting records of each institution.

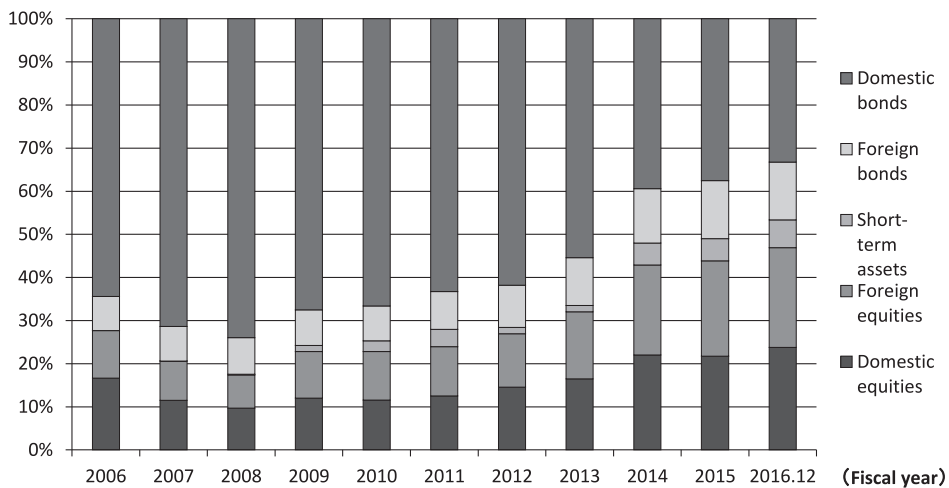
4. Voting Record of GPIF

Within these real investors, public institutions, the Government Pension Investment Fund (GPIF), and the Bank of Japan have several domestic stocks. GPIF is Japan's largest public pension. The role of GPIF is that it "shall manage and invest the Reserve Funds of the Government Pension Plans entrusted by the Minister of Health, Labour and Welfare, and shall contribute to the financial stability of both Plans by remitting profits of investment to the Special Accounts for the Government Pension Plans."⁵

In 2014, GPIF changed the policy asset mix and bought many domestic equities (Figure 7). In the current security market in Japan, the influence of public institutions is growing. As discussed earlier, asset owners (GPIF) entrust their asset management and votes. However, GPIF requested all the external asset managers of investment in domestic equities to report their stewardship activities.

Figure 8 shows the voting records of GPIF. GPIF also cast dissenting votes in 2015 and 2016. As much as 8.3% and 7.9% of the votes cast dissented to the approval of a proposed measure.

Figure 7 Investment Assets and Portfolio Allocation of GPIF



(Source) GPIF home page, <http://www.gpif.go.jp/en/>.

⁵ GPIF home page, <http://www.gpif.go.jp/en/about>.

Figure 8 Voting Records of GPIF

Proposal		Fiscal year 2015		Fiscal year 2016 (From April to June)	
		Approved	Opposed	Approved	Opposed
Proposal pertaining to company organization	Appointment of directors	92.9%	7.1%	93.2%	6.8%
	External directors	86.8%	13.2%	89.6%	10.4%
	Appointment of auditors	85.4%	14.6%	85.8%	14.2%
	External directors	79.2%	20.8%	79.2%	20.8%
	Appointment of accounting auditors	100.0%	0.0%	99.6%	0.4%
Proposals pertaining to director remuneration, etc.	Director remuneration	97.5%	2.5%	97.9%	2.1%
	Director bonuses	96.9%	3.1%	96.8%	3.2%
	Director retirement benefits	44.8%	55.2%	44.8%	55.2%
	Granting of stock options	81.1%	18.9%	85.4%	14.6%
Proposals pertaining to capital management (excluding items pertaining to amendment of the articles of incorporation)	Dividends	96.1%	3.9%	96.3%	3.7%
	Acquisition of treasury stock	100.0%	0.0%	100.0%	0.0%
	Mergers, acquisition, etc.	98.2%	1.8%	98.7%	1.3%
Proposals pertaining to amendment of the articles of incorporation		96.5%	3.5%	97.0%	3.0%
Poison Pills (Rights plan)	Warning type	46.5%	53.5%	43.7%	56.3%
	Trust-type	0.0%	0.0%	0.0%	0.0%
Other proposals		94.0%	6.0%	87.7%	12.3%
Total		91.7%	8.3%	92.1%	7.9%

(Source) GPIF home page, <http://www.gpif.go.jp/en/>.

5. Dialogues by Institutional Investors

One important activity that enhances the medium- to long-term investment returns of institutional investors' clients and beneficiaries is dialogue. Situations that result in dialogues between institutional investors and investee companies were investigated.

As the result, four out of six institutions including insurance companies and those with pension funds wholly entrusted the asset managers with the responsibility of holding dialogues. Nevertheless, almost all investment managers and trust banks have dialogues (Figure 9).

“Certain Standard” pertains to investee companies concerned with decreasing shareholder return (e.g., low distribution and introduction of takeover defense) or only active management brands. As some studies indicate, passively managing brands while adhering to Japan’s Stewardship Code is a challenge for institutional investors.

Figure 9 Situations of Dialogue

Options		Total		Investment managers and trust banks		Pension funds and insurance companies	
		Quantity of responses	Rate	Quantity of responses	Rate	Quantity of responses	Rate
① Practice by (almost) all investee companies		13	44.8%	13	56.5%	0	0%
② Practice by only poorly performing investee companies		0	0%	0	0%	0	0%
③ Practice by certain standard		9	31.0%	8	34.8%	1	17%
	③-1 Investee companies which could be concerned about decrease shareholder return (e.g. low distribution, introduction of takeover defense)	3	33.3%	2	25.0%	1	100%
	③-2 Others	5	55.6%	5	62.5%	0	0%
④ Doesn't practice dialogue on one's own		7	24.1%	2	8.7%	5	83%
Cause for	④-1 Judge based on voting policy	1	14.3%	0	0%	1	17%
	④-2 Leave entirely up to asset managers	5	71.4%	1	4.3%	4	67%
	④-3 Leave entirely up to SAAB	0	0%	0	0%	0	0%
	④-4 Others	1	14.3%	1	4.3%	0	0%
Total		29	100%	23	100%	6	100%

(Note) N = 29. As a non-response institution, the numbers of ③ (9) and ③-1 + ③-2 (8) do not sum up.

The rate and frequency of dialogue with investee companies were also studied (Figure 10). Institutional investors have dialogues with as few as one or two companies or as many as a 1,000. The frequency of dialogues per company is as follows:

Six institutions hold one or two times per year (17.65%)

One institution holds two or three times per year (5.88%)

Four institutions hold three or four times per year (23.53%)

Three institutions hold over four times per year (17.65%)

Figure 10 Rates and Frequencies of Dialogues with Investee Companies

	() % of all investee companies	About () companies of all investee		About () times per one company, one year				
				① ~ 1 time	② 1 ~ 2 times	③ 2 ~ 3 times	④ 3 ~ 4 times	⑤ 4 times~
Average	59.1%	350	Total	3	6	1	4	3
Median	55.0%	165						

(Note) N = 17. Counting only corresponds to institutions who responded.

Although the frequency of dialogues depends on each institution, many Japanese institutional investors proactively have dialogues.

With regard to the content of the dialogues, there are three options ranked as follows:

① confirmation of companies' situations (to catch up on their situation; 1.5833); ② proposals on how to increase enterprise value or exercise IR (2.1389); and ③ promote change of management policy (e.g., low distribution and introduction of takeover defense; 2.2778) (Figure 11).

Principle 3 of Japan's Stewardship Code states, "institutional investors should monitor investee companies so that they can appropriately fulfill their stewardship responsibilities with an orientation towards the sustainable growth of the companies."⁶ Japanese institutional investors intend to fulfill their stewardship responsibilities by monitoring companies' situation.

Figure 11 Content of Dialogues

Options	Average of the ranks
Confirmation of companies' situations (to catch up on their situation)	1.5833
Proposals of how to increase enterprise value or exercise IR	2.1389
Encouragement of changing management policy (e.g. low distribution, introduction of purchase defense)	2.2778

(Notes) 1. N = 17. Counting only corresponds to institutions who responded.

2. 5% significance (Friedman test).

⁶ The Council of Experts Concerning the Japanese Version of the Stewardship Code (2014), P6.

6. Conclusion

The present study investigates the activities of the accounts managers monitored by investee companies by checking the voting records and dialogues of institutions that follow Japan's Stewardship Code.

Not all real investors (institutional investors) cast affirmative votes for all measures irrespective of performance. Many institutional investors set guidelines for voting or carefully examine each shareholder measure to fulfill their stewardship responsibilities. If asset owners entrust their management or administration, they (asset owners) engage with trustees (asset managers) to decide on the vote in light of the results of the monitoring of investee companies and dialogue with them. For example, GPIF requested all the external asset managers of investment in domestic equities to report on their stewardship activities.

Although the frequency of dialogues depends on each institution, many Japanese institutional investors proactively have dialogues. Japanese institutional investors (real investors) have changed to engage with investee companies.

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